

*This document presents, in summary and simplified form, a description of the provisions of the MSA. It is not intended to interpret any of the provisions of the MSA and is not intended as a guide for such interpretation and no party should rely on any statement in this summary as a basis for action. In the event of a conflict between this document and the language of the MSA itself, the MSA governs.*

**This summary was prepared by the National Association of Attorneys General**

# **MASTER SETTLEMENT AGREEMENT SUMMARY FOR ATTORNEYS GENERAL**

## **ORIGINS OF THE MASTER SETTLEMENT AGREEMENT**

- Beginning in 1994 many States brought suit against the major tobacco companies alleging that cigarette smoking had imposed massive costs upon the States and that the companies were legally responsible for such costs. The lawsuits asserted many theories of liability including violations of state antitrust and consumer protection law. Most states' damage allegations included the Medicaid costs imposed on the State by cigarette smoking.
- In 1997 the major tobacco companies reached separate settlement agreements with four states, Mississippi, Minnesota, Florida and Texas. Later, the 46 other states, the District of Columbia, Puerto Rico and four US Territories ("the Settling States") reached a settlement agreement with the companies. This settlement agreement required federal legislation but the Congress failed to pass such legislation.
- In 1998 the Settling States and the tobacco companies reached a different settlement agreement that did not require enactment of federal legislation to become effective. This agreement, the Master Settlement Agreement ("the MSA"), was executed on November 23, 1998. In each state the court with jurisdiction over the case entered a negotiated consent decree in connection with the settlement. The consent decrees are final in all Settling States.

## **OVERVIEW OF THE MSA**

- The original parties to the MSA were the Settling States and the four major US tobacco companies, Philip Morris, R.J. Reynolds, Brown & Williamson, and Lorillard. These companies are known as Original Participating Manufacturers ("OPMs"). Since then, more than 30 other companies have joined the MSA. These companies are known as Subsequent Participating Manufacturers ("SPMs").
- The Participating Manufacturers agreed to three important sets of obligations.
  - Public health provisions that restrict the advertising, promotion and marketing of cigarettes.

- Creation and funding by the companies of the American Legacy Foundation, an organization devoted to public education and counter-advertising regarding cigarette smoking.
- Payments to be made each year by the companies to the states in perpetuity. At the time of the settlement, the present value of the payments between 1999 and 2025 was estimated at \$206 billion.
- The payment and public health provisions of the MSA obligate the Participating Manufacturers in perpetuity. The MSA never expires.
- In exchange for these commitments from the Participating Manufacturers the Settling States agreed to release their claims against the Participating Manufacturers. The MSA releases only the claims of the Settling States. The MSA does not release potential claims of individuals or classes of individuals or of the federal government. The Settling States did not release any of their claims against companies that did not enter into the MSA (“Non-Participating Manufacturers” or “NPMs”).

## **PUBLIC HEALTH INITIATIVES**

### *Prohibits Youth Targeting*

- Prohibits targeting youth in advertising, promotions, or marketing.
- Bans industry actions aimed at initiating, maintaining or increasing youth smoking.

### *Bans Cartoon Characters*

- Bans use of cartoons in the advertising, promotion, packaging or labeling of tobacco products.

### *Restricts Sponsorships By Brand Names*

- Limits tobacco companies to only one brand name sponsorship per year (after current contracts expire or after three years – whichever comes first).
- Prohibits brand name sponsorship of events with a significant youth audience.
- Prohibits sponsorship of team sports (football, basketball, baseball, hockey or soccer).
- Prohibits sponsorship of events where any of the paid participants or contestants are underage.
- Allows corporate sponsorship of athletic, musical, cultural, artistic or social events as long as the corporate name does not include the brand name of a domestic tobacco product.
- Bans tobacco brand names for stadiums and arenas.
- Limits outdoor advertising for sponsored events to the site of the event.

### *Bans Outdoor Advertising*

- Bans all outdoor advertising, including: billboards, signs and placards in arenas, stadiums, shopping malls, and video game arcades.
- Limits advertising outside retail establishments to 14 square feet.
- Bans transit advertising of tobacco products.

### *Bans Placement of Tobacco Products*

- Bans payments to promote tobacco products in movies, television shows, theater productions or live performances, live or recorded music performances, videos and video games.

### *Bans Sale of Merchandise With Tobacco Brand Names*

- Bans distribution and sale of apparel and merchandise with brand-name logos (caps, T-shirts, backpacks, etc.).

### *Bans Youth Access To Free Samples*

- After November 23, 1998, free samples cannot be distributed except in a facility or enclosed area where the operator ensures no underage person is present.

### *Bans Proof of Purchase Gifts*

- Bans gifts without proof of age (legible driver's license certified to be valid by the gift recipient). Effective November 23, 1999.

### *Prohibits Third Parties from Using Tobacco Brand Names*

- Tobacco companies are prohibited from authorizing third parties to use or advertise brand names in any way prohibited by the agreement.
- Tobacco companies must designate a contact in each state who will respond to Attorney General complaints of prohibited third party activity.
- Exempts licensing agreements or contracts in existence as of July 1, 1998, although contracts cannot be extended beyond current terms.

### *Bans Non-Tobacco Brand Names*

- Bans future cigarette brands from being named after recognized non-tobacco brand or trade names (such as Harley Davidson, Yves Saint Laurent, and Cartier) or nationally recognized sports teams, entertainment groups or individual celebrities.

### *Minimum Pack Size*

- Tobacco companies are prohibited from opposing state legislation which bans the manufacture and sale of packs containing fewer than 20 cigarettes.

## **CHANGES THE CORPORATE CULTURE**

### *Requires Corporate Commitments To Reduce Youth Access and Consumption*

Companies must:

- Develop and regularly communicate corporate principles that commit to complying with the Master Settlement Agreement and reducing youth smoking.
- Designate executive level managers to identify ways to reduce youth access and consumption of tobacco.
- Encourage employees to identify additional methods to reduce youth access and youth consumption.

## **DISBANDS TOBACCO TRADE ASSOCIATIONS**

- Disbands the Council for Tobacco Research (CTR), the Tobacco Institute (TI), and the Council for Indoor Air Research (CIAR).
- Requires all records of these organizations that relate to any lawsuit to be preserved.

### *Provides Regulation and Oversight of Any New Trade Organizations*

Requires any new trade association to adopt bylaws that provide:

- Officers of the association will be appointed by the board, be employees of the association and will not be employed by a member tobacco company;
- Legal counsel will be independent and not serve as counsel to member companies;
- Minutes of board of directors meetings will be prepared and maintained for at least five years.
- Antitrust staff for any settling state may inspect and copy all non-privileged, non-work-product records and interview association directors, officers and employees.

## **RESTRICTS INDUSTRY LOBBYING**

### *Stops Industry Assault On Tobacco Control Laws*

- After state specific finality, tobacco companies will be prohibited from opposing proposed state or local laws or administrative rules which are intended to limit youth access to and consumption of tobacco products.
- The industry must require its lobbyists to certify in writing that they have reviewed and will fully comply with settlement terms including disclosure of financial contributions regarding lobbying activities and new corporate culture principles.
- In states without laws regarding financial disclosure of lobbying, requires disclosure of lobbying costs to the state Attorney General.
- Prohibits the industry from lobbying for the diversion of settlement money to non-tobacco or non-health related uses or legislation which would eliminate or diminish state rights under the settlement.

### *Protects State and Local Youth Access Laws*

- Prohibits new challenges by the industry against the enforceability or constitutionality of tobacco control laws, ordinances, and rules passed prior to June 1, 1998.

### *Dismisses Lawsuits Against State Laws*

- Requires the industry to dismiss, without fees, all claims against participating states.

### *No Criminal Immunity*

- Specifies that states expressly do not waive any right to pursue criminal prosecutions based on federal, state, or, local law.

## **OPENS INDUSTRY RECORDS AND RESEARCH**

### *Opens Public Access To Tobacco Documents*

- Tobacco companies will release documents that are under protective orders in state lawsuits and have no privilege or trade-secret claim.
- Settling states may seek court-approved release of any documents which have been subject to an order or ruling, prior to August 17, 1998, denying privilege, work-product or trade secret protection. The industry can contest the action.

### *Creates User-Friendly Website For Industry Documents*

- Requires tobacco companies to maintain for ten years, at their expense, a Website which includes all documents produced in state and other smoking and health related lawsuits.
- Requires the industry to maintain the site in a user-friendly and searchable format (requires an index and other features to improve searchable access).
- Requires the industry to add to the website, at its expense, all documents produced in future civil actions involving smoking and health cases.
- The industry will provide the National Association of Attorneys General with up to \$100,000 for a computer consultant to ensure that the industry's Website is truly usable.

### *Stops Conspiracy To Hide Research Regarding Smoking and Health*

Prohibits manufacturers from jointly contracting or conspiring to:

- Limit information about the health hazards from the use of their products;
- Limit or suppress research into smoking and health; or
- Limit or suppress research into the marketing or development of new products.
- Prohibits the industry from making any material misrepresentations regarding the health consequences of smoking.

## **CREATES A FOUNDATION AND \$1.45 BILLION PUBLIC EDUCATION FUND**

### *Establishes American Legacy Foundation to Engage in Public Education and Anti-Tobacco Advertising Programs*

- Pursuant to the MSA, The NAAG Executive Committee provided for creation of the foundation.
- The foundation is governed by an eleven-member board of directors. NAAG, the National Governors' Association and the National Conference of State Legislatures each appointed two board members and these six selected the final five members, four of whom have expertise in public health, medicine and child psychology. The board members elected by NAAG are Attorneys General Gregoire and Sorrell.

### *Functions of the Foundation*

- Carry out a nationwide, sustained advertising and education program to counter youth tobacco use and educate consumers about the cause and prevention of diseases associated with tobacco use. The foundation is prohibited from engaging in political or lobbying activities.
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- Develop, disseminate and test the effectiveness of counter advertising campaigns.

- Develop, disseminate and test the effectiveness of model classroom educational programs, including programs targeting at-risk populations.
- Develop, disseminate and test the effectiveness of criteria for effective cessation programs.
- Commission studies, fund research and publish reports on factors that influence youth smoking and substance abuse.
- Develop targeted training and information programs for parents.
- Maintain a library of foundation studies, reports and publications.
- Track and monitor youth smoking and substance abuse with a focus on reasons for increases or failures to decrease tobacco and substance abuse rates.

### *Programs to Reduce Teen Smoking and Substance Abuse*

- Requires the industry to pay \$25 million annually from 1999 through 2008 to support the study of programs to reduce teen smoking and substance abuse and the prevention of diseases associated with tobacco use.

### *National Public Education Fund*

- The agreement requires the industry to pay \$1.45 billion over the five year period 1999-2003 for a National Public Education Fund administered by the American Legacy Foundation.
- The agreement authorizes continued funding after 2003 if in any year the share of the total U.S. cigarette market held by the tobacco product manufacturers who have agreed to be bound by the Agreement equals or exceeds 99.05%. This condition currently seems unlikely to be met for any future year.
- The fund is established to carry out a nationwide sustained advertising and education program to counter youth tobacco use and educate consumers about tobacco-related diseases. The fund is not to be used for vilification of individuals or companies.
- The fund may make grants to states and political subdivisions to carry out the fund's purposes. The Foundation has made a wide range of grants to the states.
- Outside contributions can be made to the foundation and specifically to the education fund.

## **ENFORCEMENT**

### *Provides Court Jurisdiction For Implementation and Enforcement*

- A single court is established in each Settling State with exclusive jurisdiction to enforce Agreement and consent decree and each tobacco company signatory submits to the jurisdiction of each state court.
- A state is not required to give any prior notice before seeking an order to enforce a consent decree from the court – except that a 10-day notice is required if the claimed violation involves targeting youth or making material misrepresentations

about tobacco products (unless the Attorney General determines there is a public health or safety concern requiring faster action, or the party has committed substantially similar violations previously).

- If the court finds the consent decree has been violated, the court may award any relief available under the consent decree or the law in that state.
- Settling states may also apply to the court to enforce or interpret the terms of the Agreement, although such a state must give the other parties and NAAG 30-days prior notice (unless the Attorney General determines there is a public health or safety concern requiring faster action).
- If the court issues an enforcement order enforcing the agreement and a party violates that order, the court may order monetary, civil contempt or criminal sanctions to enforce compliance with the enforcement order.
- Allows settling state AGs access to company documents, records and personnel to enforce the agreement irrespective of a judicial enforcement proceeding, if there is reasonable cause that a violation of the agreement has occurred.

### *NAAG Provides Implementation And Enforcement Coordination*

NAAG is to

- Coordinate and facilitate implementation and enforcement of the agreement on behalf of the AGs.
- Monitor potential conflicting court interpretations involving the settlement.
- Convene two meetings each year and one national conference every three years to evaluate the success of the settlement and coordinate AG efforts.
- Assist states with inspection and discovery activities which are conducted to enforce the settlement.
- Assist states in defending legal challenges to the agreement.

### *State Enforcement Fund Established*

- On March 31, 1999, the industry paid \$50 million to establish a fund to assist Settling States in enforcing and implementing the agreement and to investigate and litigate potential violations of state tobacco laws.

## **PAYMENTS**

*MSA Provides for Base (unadjusted) Payments Estimated at the Time of Execution to Have A Present Value of \$206 Billion Through 2025.*

- Participating Manufacturers make payments to a single set of accounts for all Settling States and the American Legacy Foundation pursuant to directions from an independent auditor, which calculates the payments.
- Distributions to the States are based on percentages agreed to by the States (Exhibit A).



### *Initial Payments*

- The MSA provides for five (5) initial *base* payments by the OPMs in January of each year, 1999-2003, subject to adjustments. The final initial payment is due on January 2003. The base amount of the five payments totaled \$12.5 billion but due to adjustments provided for in the MSA (some of which are being disputed); the actual initial payments received by the States to date have been substantially less. After January 2003 there will be no further Initial Payments.

### *Annual Payments*

- Annual *base* payments due April 15 of each year in perpetuity commenced with a scheduled base payment in 2000 of \$4.5 billion. Scheduled annual base payments for 2001 and 2002 were \$5 billion and \$6.5 billion respectively. However, due to upward and downward adjustments provided for in the MSA (some of which are being disputed); the actual annual payments received by the States have been substantially less. Future annual base payments are scheduled as follows:
  - 2003: \$6.5 billion
  - 2004-2007: \$8 billion
  - 2008-2017: \$8.139 billion (plus \$861 million to the strategic fund)
  - 2018 forward: \$9 billion
  - Payment calculations are made by an independent auditor (PricewaterhouseCoopers) paid for by the industry and by a fund established in the agreement.

### *Strategic Contribution Fund Payments of \$8.610 Billion*

- On April 15, 2008 and on April 15 each year through 2017, the companies will pay \$861 million into a strategic contribution fund.
- Money from the fund will be allocated to states based on a strategic contribution formula developed by the Attorneys General. The allocation formula reflects the contributions made by states toward resolution of the state lawsuits against tobacco companies (Exhibit U).

### *Additional Payments*

- Payments to the Foundation of \$25 million annually, 1999-2008 (see discussion above)
- Payments to the National Public Education Fund at least totaling \$1.45 billion between 2000 and 2003 (see discussion above)
- One-Time Payment of \$50 million into Attorney General Enforcement Fund in 1999

- Payments to NAAG for Administrative Expenses of \$150,000 annually, 1999-2008.

### *Adjustments Provisions*

- Annual payments are adjusted annually based on an inflation factor. (The greater of the percent % increase in the CPI, compounded annually, or 3%.) Because of annual compounding and the 3% floor, Inflation Adjustment will increase payments in 2003 by over 13%.
- The amounts of the annual payments are subject to “volume adjustments.” Payments by Participating Manufacturers are decreased if sales by Participating Manufacturers are below the base level of 1997. Since 1997, sales by Participating Manufacturers have declined by approximately 20 percent. In 2002 payments were reduced by approximately \$1.2 billion because of the volume adjustment.
- Annual payments also are subject to a reduction by the settlement share amounts which have been allocated to the four states that did not join in the Agreement, but rather settled separately.

### *Non-Participating Manufacturer Adjustment*

- If the aggregate share of the national cigarette market of Participating Manufacturers decreases in any year by more than two percent from those companies’ aggregate market share in 1997 (“Market Share Loss”), the companies’ annual payment is potentially subject to a reduction of three percent for each percent of Market Share Loss. In other words, a gross decline in the companies’ market share of five percent could result in a Market Share Loss of three percent and a reduction in the annual payment of nine percent (5% less 2% times 3). This is known as the “NPM Adjustment.”
- Even if there were a Market Share Loss in any year, there would be no NPM Adjustment unless a national economic consulting firm chosen by the States and the tobacco companies determined that the disadvantages caused by the MSA were a significant factor contributing to the Market Share Loss. Such a firm, headed by a Nobel laureate in economics, has been selected and is expected soon to begin the process of making this determination for the 1999 NPM Adjustment.
- Even if there were a determination that the MSA’s disadvantages were a significant factor contributing to a Market Share Loss in any year, a State would still not be required to bear any portion of the NPM Adjustment if the State had been “diligently enforcing” its so-called Model Statute or Escrow Statute (Ex. T to the MSA) during that year. All States have passed a Model Statute. None has had its enforcement of the Statute challenged in court, although a few tobacco companies have indicated intent to do so.
- If a State’s Model Statute were ruled unconstitutional, the State’s share of the annual payment could be reduced by the NPM Adjustment by no more than 65 percent.

## **MODEL STATUTE**

- Every Settling State has enacted a Model Statute in substantially the form of Exhibit T to the MSA. Under the Statute, every Tobacco Product Manufacturer selling cigarettes in the state must either become a Participating Manufacturer under the MSA or pay a specified amount per cigarette into an escrow account. If a company becomes a Participating Manufacturer, it is released from liability to the State. If it chooses not to join the State does not release it from liability. The purpose of the escrow fund is to ensure that a State that ultimately sues and recovers from a Non-Participating Manufacturer will have a fund available against which to recover. The escrow funds remain the property of the manufacturer and the manufacturer is entitled to take out on a current basis the interest earned on the escrow account.
- The Model Statute is also designed to prevent companies that do not become Participating Manufacturers and therefore do not incur the cost of the settlement payments from enjoying a windfall benefit by selling its cigarettes without taking into account the costs that smoking imposes on the State.

## **COST RECOVERY AND ATTORNEY FEES**

### *States Recover Cost, Expenses and Market Rate for Attorney Fees*

- Participating Manufacturers Paid \$150 million to Settling States for in-house attorneys fees and costs incurred in the litigation. After full payment to the Settling States, the remaining amount of almost \$50 million was committed to a Foundation to be used to support the defense and enforcement of the MSA and for other purposes.

### *Outside Attorney Fees*

- Two payment methods are available – liquidated fee agreement and arbitration.
- Some outside counsel have negotiated a liquidated fee agreement with the industry, and where accepted, are being paid from a \$1.25 billion pool of money from the tobacco industry over four years. If outside counsel accepts a liquidated fee, they must release the state from all claims for attorney fees.
- Outside counsel that reject the liquidated fee process or cannot agree to an offer can go through arbitration.
- A three-member arbitration panel was established with two permanent members and a member from the state represented by the outside counsel.
- The industry must pay whatever arbitrators award, but the timing of the payment will be subject to a \$500-million-per-year cash flow cap.

## **MISCELLANEOUS PROVISIONS**

### *Most Favored Nations Provisions*

- If a tobacco company and a governmental entity enter into a settlement agreement with non-economic terms that are more favorable than those of the MSA, the MSA will be revised as to such tobacco company to include the more favorable non-economic terms.
- If a settling state enters into a settlement agreement with a tobacco company that is not a party to the MSA (Non-Participating Manufacturer or “NPM”) and the overall terms of such agreement are more favorable to the NPM than are the terms of the MSA, the MSA will be revised as to the original signatory tobacco companies to incorporate the more favorable overall terms.
- If any settling state agrees to relieve any company that is a party to the MSA from any part of its payment obligation, then as to such settling state the MSA will be revised to provide all other signatory tobacco companies the same payment relief.

### *Settlement Amendment Provisions*

- The settlement can be amended in writing only if all affected states and all affected companies agree to the amendment.